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E-COMMERCE TAXATION IN INDIA: Tax Havens vis-a-vis Indo Mauritius DTAC

Hitendra Hiremath & Netra Koppad

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E-COMMERCE TAXATION IN INDIA: Tax Havens *vis-à-vis* Indo-Mauritius DTAC

Hitendra Hiremath Netra Koppad***

[**Abstract**: *The present study aims to bring forth the flaws in the existing Taxation Laws in India. It primarily focuses on the ongoing Indo- Mauritius DTAC. It delves upon various guidelines issued by International Organizations, Judicial Pronouncements by Courts, etc. Further, the article underlines the major problem of determining the permanent establishment of these entities. Discussing the other pertinent drawbacks of the E-Commerce Tax regime the article also suggests various measures to overcome them, which could help to boost the Indian economy*.]

I

Introduction

The world has entered into a digital age, where transacting business with information technology and computer system as a tool is preferred over the conventional methods. The World Trade Organisation defines *E-Commerce* as *understood to mean the production, distribution, marketing, sale or delivery of goods and services by electronic means*.[1] Succinctly, any form of the business which actually uses technology as a tool in order to facilitate the transaction can be referred to as '*E-Commerce*'.

Regulating E-Commerce has always been a daunting task for countries across the globe. International Organizations have time and again laid down rules for governing E-Commerce. India has not been lagging behind and has also framed regulations governing the same. The difficulty that has persisted over time is how to levy tax on these the E-Commerce entities. The ambiguity is whether to levy the tax based on the source of income or on permanent establishment. What happens when these entities have establishments scattered around the world? In such cases different countries levy the taxes over same income twice which poses the problem of '*Double- Taxation*'. To overcome this issue of double- taxation a tax treaty is signed between two or more countries known as Double-Tax-Avoidance Convention (hereinafter referred as DTAC).

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* Principal Associate and **Legal Consultant, RERA Consultants. *Emails*: hitendrahiremath@gmail.com.; netra.k2905@gmail.com.

1 Council for Trade-Related Aspects of Intellectual Property Rights, *Note by Secretariat: The Work Programme on Electronic Commerce,* WTO Doc. IP/C/W/128 (February 10, 1992).

The present study aims to bring forth the flaws in the existing Taxation Laws in India. It primarily focuses on the ongoing Indo-Mauritius DTAC. It delves upon various guidelines issued by International Organizations, Judicial Pronouncements by Courts, etc. Further, the article underlines the major problem of determining the permanent establishment of these entities. Discussing the other pertinent drawbacks of the E-Commerce Tax regime the article also suggests various measures to overcome them, which could help to boost the Indian economy.

Part II discusses the taxation scheme on non-residents in India under the Income Tax Act, 1961. Part III summarizes the taxation on the basis of the notice by the Central Board of Direct Taxes, followed by a detailed understanding of Permanent Establishment (hereinafter referred to as the PE) as per the OECD guidelines and judicial pronouncements in India in Part IV & V. Part VI delineates the concept of tax havens and the role of the treaty between India and Mauritius in dealing with the issues related to taxation in e-commerce.

II

Taxing Non-Residents: Income Tax Act 1961

Levying taxes on residents or entities that have permanent establishments situated within the territorial boundaries of India has always been unchallenging. On the other hand, levying taxes on non-residents has been a demanding task. Income Tax Act, 1961 (hereinafter referred as '*IT Act*') lays down the provisions regulating taxation of non-residents. The provisions are Sections 4, 5, 6 and 9 of IT Act. Briefly, the income of a non-resident is to be taxed in India if his income accrues in India or if it has been received in India.[2]

'Residential Status'- Section 6 IT Act

Section 6 of the IT Act lays down the conditions to be fulfilled to prove residential status. It includes conditions that needs to be fulfilled for ascertaining residence of the 'persons'[3] as well as companies. In the case of individuals, the period of stay is taken into account and a company is considered to be a resident if it is registered in any of the previous years under the Companies Act or any other law which is in

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[2] Central Board of Direct Taxes on E-commerce, *Report of the High Powered Committee* (2001), available at - http://www.rashminsanghvi.com/downloads/taxation/international-taxation/bpo_taxation_in_india/Annexure_1-Taxation_of_non-residents.pdf(last visited Jan. 20, 2019).

[3] *See also*, section 2(31), The Income Tax Act, 1961.

force for time being or that the company has its place of effective management in India.

The moot point has always been determining the residential status of the companies involved in the E-Commerce business. There are companies which are situated outside India but their place of functioning that is 'Permanent Establishment' exists within its territorial borders. In such cases a Tax Treaty or DTAC becomes imperative to avoid the problem of double-taxation. The residential status of such companies is considered from where they effectively carry on their business or their Permanent Establishment' and these entities are taxed accordingly.

Income Chargeable to Tax: Section 5 IT Act

Section 5(2) of the IT Act provides that:

> Subject to the provisions of the said Act, the total income of the person in any of the previous year who is non- resident in such year shall include all the income, profits, gains from whatever source they are derived which:
>
> a. were deemed or received in India by the person or on behalf of him, or
> b. accrued or arose or deemed to accrue in India during that year

The explanation appended to Section 5 of the IT Act clarifies that income accruing or arising outside India shall not be deemed to be received in India for the only reason that it is considered in the balance sheet which was prepared in India.

Thus, it can be interpreted that if such amount is received by or on behalf of the non-resident in India, even if it is accrued outside India then it is to be taxed in India. In ***P.V. Raghava Reddi***[4] case, Supreme Court upheld the High Court's decision, treating the appellant as 'statutory agent' of the Japanese company and the commission credited to a Japanese account from the orders of that firm, were deemed to be received in India as the transaction was made and credited to its account at the behest of the instructions given by it. Thus, it was held that the Income-tax authorities correctly assessed the appellant on the amount received for the two account years.

The Government of India has entered into several DTAC's with other nations to overcome the problem of double-taxation. Various provisions of IT Act are applicable while levying of taxes. On the other hand, if there are provisions of

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4 *P.V. Raghava Reddi* v. *CIT*, 1962 A.I.R. S.C. 977.

DTAC's that are more beneficial to the assessee then the latter will have an overriding effect on the former.[5]

'Income Accruing or Arising in India': Section 9, IT Act

Section 9(1) of the IT Act deals with the Income accruing or arising in India and it states that:

> 'all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, [* * *] or through the transfer of a capital asset situated in India'.

The explanation appended to Clause (i) provides that only that part of business income is taxable in India which is carried through India. However, the exemption is provided to the non-residents if they purchase any goods in India for the purpose of exports.

Further *Explanation 2* also mentions that 'business connection' shall include any business activity carried out through a person who, acting on behalf of the non-resident keeps the stock of merchandise for delivering it to any other person. Then the same shall be said to have accrued in India.

Supreme Court has also discussed the term '*business connection*' in various case laws, in order to ascertain income accruing or arising in India. In *CIT* v. *TIM Sales Ltd*,[6] where the company in India acted as organization for marketing of the products of foreign companies, the Supreme Court cited the following reasons and held that there is no 'business connection' with the foreign companies by the Indian Companies:

- That the raw materials and the finished products were produced outside India;
- The contract was entered between the parties outside India and the actual amount was received outside India;
- Delivery of the finished goods to the consumers were also made outside India;
- The orders were only accepted in India, but the actual business took outside i.e., in London;
- Intimation was made to the consumers by the company which is situated outside India, even though the consumers are from India;
- However, the Indian company was not having any authority to accept the offers but it merely communicated the offers to the company situated in London which made the real acceptance of the offers.

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5 *See*, section 90 (2) of The Income Tax Act, 1961 (Act No. 43 of 1961). *See also, CIT* v. *Vishakhapatnam Port Trust*,(1983) 144 I.T.R. 146 AP paras 22,32, and 40.

6 *CIT* v. *TIM Sales Ltd.*,1987 A.I.R. S.C. 1234, para 6.

However, Advance Authority Ruling (AAR) came out with the contradictory view in, *In Re: Advance Ruling P. No. 8 of 1995.*[7] Here a company was incorporated in Switzerland, and it was in the business of trading goods and other commodities of an international stature in India. The company intended to setup its subsidiary company in India to provide consultancy services from India to foreign companies for use outside India. The Indian subsidiary company was to be used by the foreign company as a subsidiary. The authority referring to the judgment given by the Supreme Court in *R D Aggrawal* and *Tim Sales case*[8] pointed out that the type of the relationship between the companies is completely different and the company which is tendering the assistance is the subsidiary company. It is under the direct control of the Swiss company as it had to follow the instructions of the Swiss company and also 'act as his agent' in the tender process. The AAR pointed out that the continuous relationship with a foreign company shall constitute a 'business connection' for the purposes of the Sec. 9 (1) (i) of the IT Act. The supply of the technical information and knowhow about the manufacturing of products by the foreign company to an Indian company was considered as the 'business connection'. The technical fees and royalty were deemed to be accrued in India.[9]

Attribution of Income

The Income Tax Rules of 1962 vide Rule 10, points that there can be determination of the income which is actually carried in India or attributed in India. However, in case business of non-resident is carried in India or partially outside India, authorities were of the opinion that it is hard to ascertain the nature of such income. In this circumstance:[10]

- the percentage of the total turnover of the company wherein the revenue authorities deemed to consider as a reasonable one;
- the total receipts which are accruing or arising to that company from the business done in India;
- the revenue authorities need to take the final call as the percentage of the gains that need to be taxed of such company were taken into account.

III

Taxing Of 'Non-Residents': Circulars by CBDT

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7 *In Re: Advance Ruling P. No. 8 of 1995*, (1997) 223 I.T.R. 416 AAR paras2 and 4.

8 *Supra*, note 5.

9 *Carborendum Co* v. *CIT*, 1977 A.I.R. S.C. 1259.

10 *Supra* note 6, para 8.

Two circulars were issued by Central Board of Direct Taxes (hereinafter referred as CBDT) relating to taxing of the non-resident. One was issued under 'section 9 of the IT Act' and another was issued on 'taxing of non-residents based on the Permanent Establishments'. It is pertinent to note the relevant portions of the mentioned Circulars:

Circular No: 23: This circular, issued dated, 23/7/1969, deals with non-residents (individual, exporter, importer and a company's business) connection in India and their liabilities as per Indian taxation laws.

> **1.** *Non-residents-Income accruing or arising through or from business connection in India-Liability to tax-Section 9 of the Income-tax Act, 1961.*
>
> *Sec. 9 of the Income-Tax Act corresponding with Sec. 42 of the Indian Income-tax, 1922 provides that the income arising directly or indirectly from or through any business connection in India shall be deemed to be income accruing or arising in India, where a non-resident is entitled to such income, it will be includible in his total income.*
>
> **2.** *The term import and the expression 'business connection' have been explained by the Supreme Court in C.I.T. v. R.D. Aggarwal and Co. and another*[11]*. The question whether a non-resident has a 'business connection' in India from or through which income, profits or gains can be said to accrue or arise to him within the meaning of section 9 of the Income-tax Act, 1961, has to be determined on the facts of each case. However, some illustrative instances by which a non-resident having business connection in India can be determined are:-*
>
> a) *If a non-resident maintains a branch office in India for the purchase or sale of goods or transacting other business,*
>
> b) *Appointing an agent for the aforesaid reasons,*
>
> c) *Erecting a factory in India where the raw produce purchased locally is worked into a form suitable for export abroad,*
>
> d) *Forming a local subsidiary company of the non-resident parent company or having any financial association between a resident and a non-resident company.*

The Circular Number 23 by CBDT, made the income arising in India through any type of 'business connection' taxable. It further laid the conditions to determine the type business connections that are taxable and clarified the applicability of Section 9 on the transactions of the non – resident companies with Indian companies.

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[11] 1965 A.I.R. S.C. 1526.

Circular No: 1/2004: This circular was issued by CBDT for Taxation of Business Process Outsourcing Units in India. The relevant portion of the circular is furnished accordingly:[12]

> 'A non-resident or a foreign company is treated as having a permanent establishment or business connection in India under Article 5 the of Double Taxation Avoidance Agreements or under Section 9 of the Income-tax Act, 1961, if the said non-resident or foreign company carries on business in India through a branch, sales office etc., or through an agent (other than an independent agent) who habitually exercises an authority to conclude contracts, or regularly delivers goods or merchandise, or habitually secures orders in India, on behalf of the non-resident principal. In such a case, the profits of the non-resident or foreign company attributable to the business activities carried out in India become taxable under the Income-tax Act, 1961.'

These circulars are in conjunction with rules laid by International Organizations on Permanent Establishment. These circulars make it lucid that CBDT wanted to tax the entities which are involved into the business either directly or indirectly with the nation. It tried to fix the liability of the entities which are governed under the relevant provisions of the DTAC.

IV

OECD and 'Permanent Establishment'

The concept of 'Permanent Establishment' has been comprehensively dealt under the Organization for Economic Co-Operation and Development (hereinafter referred as OECD) Model Tax Convention.[13] According to it, *permanent establishment*, means

> 'a fixed place of business through which the business of an enterprise is wholly or partly carried.[14]It includes any office, its branch, the place of management of the enterprise, factory, the workshop, any place from which the extraction of the natural resources is being place.'[15]

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12 Circular No.1, *Section 9 of the Income Tax Act, 1961 – Income deemed to accrue or arise in India – Taxation of Business Process Outsourcing Units in India*, *available at*:http://incometaxindia.gov.in/Communications/Circular/910110000000000292.htm (last visited, Jan. 20, 2019)

13 OECD, *Articles of the Model Convention with Respect to Taxes on Income and on Capital*, available at - http://www.oecd.org/tax/treaties/1914467.pdf(last visited Jan. 20, 2019).

14 *Id*. Article 5(1).

15 *Id*. Article 5(2).

The relevant portion of the Article for an 'E-Commerce enterprise' is *Article 5 provision 4*.[16] It states that where the enterprise is using Permanent Establishment for storage of the goods and merchandise in order to sell it off, it shall be considered as the permanent establishment. Though such place may be used for maintenance and is for continuing the business that is auxiliary in nature.

The Article also deems the place where such person enjoys the independency of concluding the contracts of the enterprise as the 'permanent establishment'.[17]

Even a non- resident of India can be engaged in any type of business in India. The income derived through such business either directly or indirectly (that is himself or through the agent authorized on his behalf), is taxable. This is applicable to all types of income including income which are derived either through traditional or electronic means[18]. Considering the present position:

- The existing provisions do not provide for the taxability of incomes derived through electronic means;
- provisions are silent about the income attributable to the functions performed by the equipment;
- no difference amongst the provisions as to income derived from conventional or electronic means;
- the sale which takes place through the help of the electronic means is treated similar to that of the traditional ones.

A High-Powered Committee was constituted by the Government of India. It submitted its report in July, 2001. Its recommendation included adding of the new provisions for regulating taxation of E-Commerce entities.[19] Some of the Committee's major recommendations were as follows:

1) The concept of the permanent establishment should be removed. A new rule should be framed regulating the taxation of foreign enterprises. The tax shall be in the way of withholding tax with the criteria of being taxed at net income.
2) There is no necessity of differential tax treatment on various categories of income. The best solution is to do the direct taxing up on all streams of income, in a way that there is equitable sharing of the revenue between residence and source countries.

The suggestion made up by the committee fall in the lines of International Taxation law. An alternative to Permanent Establishment is present in the existing IT Act, i.e., concept of 'Business Connection' under Section 9.[20]

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16 *Id*.

17 *Id*. Article 5(5).

18 D.P. Mittal, INDIAN DOUBLE TAXATION AGREEMENTS & TAX LAWS1 (2011).

19 *Id*.

20 *See*, section 9, The Income Tax Act, 1961 (Act No. 43 of 1961).

In October 1998, Ministerial Conference was held in OECD on '*A Borderless World-Realizing the potential of Electronic Commerce*'. The conference applied the existing principles of Income Tax to the E-Commerce which are neutrality, efficiency, certainty, simplicity, effectiveness, fairness and flexibility. The Committee believed that these principles can be applied by the signatories through their local tax legislations. However, the Ottawa Conference which was also on 'E-Commerce Taxation' pointed out that there must be the difference between the tax and tariff.[21]

The following Sections of the Article depict the tendency to tax the E-Commerce Enterprises in one or other way. However, these E-Commerce Enterprises find different ways to bypass the taxation net. Difficulty is posed when they setup their enterprise in the States which are deemed to be 'Tax Havens', such as Mauritius, Singapore etc. This at times leads to huge revenue loss to the country concerned.

Question arises as to, whether mere use of the computer equipment in a particular country constitutes 'Permanent Establishment' there? In the country where the automated equipment is used can be considered as the Permanent Establishment. However, the distinction should be made if there is use of such equipment under certain circumstances for instance when data and software are used and stored in such computer.

On the other end, an internet website does not constitute a Permanent Establishment. It can be used from anywhere around the world. However, the server of such website needs to be taken into account and it shall constitute the 'Permanent Establishment'.[22]The nature of activities decide the place of the business of such enterprises which are involved in E-Commerce, if the services are core in nature then it shall constitute the permanent place.[23]

V

'*Permanent Establishment*'- Judicial Pronouncements

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21 OECD, '*Taxation and Electronic Commerce – Implementing the Ottawa Taxation Framework Conditions*', Recapping the Ottawa Conclusions, Page No. 10 & 11, *available at*:https://www.oecd.org/tax/consumption/Taxation%20and%20eCommerce%202001.pdf, (last visited Aug. 04, 2020).

22 OECD, Committee on Fiscal Affairs, *Clarification on the Application of the Permanent Establishment Definition of E-Commerce: Changes to the Commentary on the Model Tax Convention on Article 5*, available at - http://www.oecd.org/tax/treaties/1923380.pdf(last visited Aug. 04, 2020).

23 *Id*.

Permanent Establishment as defined under the IT Act and other conventions means, 'the place of business of any firm, which mean the fixed place where the business is carried on as pointed and defined under various DTAC's'.[24] In India, on other hand, the taxation of the non-residents takes place through establishment of 'Business Connection'. But, in India the profits (direct or indirect) are attributable to the enterprise Permanent Establishment and are also taxed.[25] Therefore, any Permanent Establishment which generates its profits or incomes through aid of the Business Connections in India is taxable. In certain circumstances where the Permanent Establishment is generating the income without the help of the business connection, then it shall be a 'taxable entity' and not the taxpaying entity.[26]

The DTAC's as entered by India includes three types of 'Permanent Establishments', they are:

- Fixed Place Permanent Establishment
- Agency Permanent Establishment
- Service Permanent Establishment

The Indian Courts have laid various tests to identify the types of the 'Permanent Establishment'. It includes 'The Geographic Test', 'The Test of Right of Usage' and 'The Binding Test'. They are used to determine the fixed place of 'Permanent Establishment' and the Agency and Service Permanent Establishment uses and it's the legal and economic dependency.

In the case of *Galileo International*,[27] Galileo International provided the airline tickets with the help of the agents for the travelers of India to United States of America. This was done with the help of the computerized systems at the Agent's place where the computers were controlled and managed through a master computer situated in USA. The company used to get its commission for the same at US. Income Tax Appellate Tribunal (hereinafter referred as '*ITAT*')in this case opined that the Galileo International revenue is been generated in India. Further it took account of the fact that without computers the operations could not have been carried. The fixation of the computers at agents place itself constitutes 'the Fixed Place Permanent Establishment' for Galileo International in India.

Applying the 'Geographic Test', the two conditions were fulfilled, firstly, that the computer system placed at the agent's premises is the identifiable place of

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[24] *See*, Article 5, The Indo-Mauritius DTAC.

[25] *Id*. Article 7, (relating to 'Business Profits').

[26] Jaydeep Menon, *International Taxation: The PE-dominated Horizon in India*, *available at*:http://www.taxindiaonline.com/RC2/inside2.php3?filename=bnews_detail.php3&newsid=6675, (last visited Aug. 04, 2020).

[27] *Galileo International Inc*. v. *DCIT*, (2007) I.T.A.T; Del., para 12.2.

business in India. And secondly, it contributed to the revenue generation and exclusive right in control was with the company.

In another case,[28] Rolls Royce used to supply the engines and other relevant parts through the Indian subsidiaries. These Indian subsidiaries had their premises in India. ITAT held, that the premises itself constitute the 'place of establishment'. The conditions for determining it were also fulfilled. Firstly, there was place of business and secondly, the right of usage was with Rolls Royce. The orders were taken in India at the behest of the controller i.e., the Rolls Royce.

In another landmark case of *Morgan Stanley & Company International*,[29] the company used to outsource its financial services work to its enterprise named Morgan Stanley Advantages Services Private Ltd in India. The Court upheld the ruling of the Advance Authority, as there was no fixed place of the Permanent Establishment in India. This case made history in field of International Taxation. The Supreme Court for the first time distinguished between 'stewardship' and 'deputation'. The court ruled that stewardship activities, which essentially involved supervision of the operations of the Indian entity and similar activities, were for purposes of risk mitigation and quality control for Morgan Stanley's benefit. These activities are not the same as 'rendering services' to the Indian Entity and therefore do not result in a 'Permanent Establishment' of Morgan Stanley in India. The question of how much income is attributable to the Permanent Establishment has always been contentious. One of the proposed methods for determining income attributable to the same has been the 'arm's length' basis of attribution in India. Before the Supreme Court's decision in the Morgan Stanley case, despite the fact that transactions were concluded on an arm's length basis, the income attributable to the Indian PE was still uncertain since the tax authorities could go beyond the arm's length consideration attributable to an Indian PE. The Supreme Court has put this issue to rest.[30]

The Supreme Court examined that the transfer of the work fell within the place of business of enterprise. The Court differentiated the main functions carried on by the company with that of its ancillary services which carried done by its Indian entity. Court held that the ancillary service is completely different as compared to its main service. However, Court said that there was no Permanent Establishment as there was no rendering of the services through stewardship activities. The Court

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[28] *Rolls Royce* v. *Director of Income-Tax*, (2008) 113 T.T.J. Del 446, para 21.

[29] *DIT (International Taxation)* v. *Morgan Stanley & Company International*, (2007) 9 S.C.A.L.E. 1.

[30] Annapoorna Jayaselan, *The Morgan Stanley's case: Beyond BPO's*, *available at:* https://www.livemint.com/Money/XeagRegAUexJKqymG3ZyTI/The-Morgan-Stanley-case-beyond-BPOs.html(last visited Jul. 10, 2020).

held that the Indian enterprise is the Service Permanent Establishment based on the provision under Indo-US DTAC. It said that if the employees are placed for more than certain specified period it constitutes a service Permanent Establishment. It pointed out that the company situated is responsible for the work of the deputed employees as the company had retained the lien over the engaged and employed employees.

VI

Tax Havens: Difficulties and Way Forward

Mauritius is treated as a 'Tax Haven'. A tax treaty has been signed between two-countries, India and Mauritius. Indo-Mauritius DTAC provides that there is no tax on capital gains, through sale of shares of an Indian Company by a Mauritian Company. In case of other transactions, they can be either be taxed in India or Mauritius. This usually results in huge loss of revenues to India[31].

Indian authorities have raised concerns about the Indo-Mauritius Treaty on two counts: Firstly, that offshore investors are setting up 'conduits' in Mauritius, solely to avail of Mauritius Treaty benefits without having any actual commercial purpose for setting up such entities; and secondly, that Indian residents are using Mauritius for 'round tripping' funds back into India for tax avoidance and money laundering.[32]

Round Tripping

Round Tripping involves the transfer of illegal money from India to some other nation, which is then re-routed to India by way of FDI and FII. In *Vodafone International Holdings case*,[33] Supreme Court observed that India is considered as one of the favorite destinations which attract huge Foreign Institutional Investors (hereinafter referred as 'FII') and Foreign Direct Investments (hereinafter referred as 'FDI').The Court noted that Indian Companies by creating shell companies in Mauritius manage to obtain a Tax Residency Certificate (hereinafter referred as 'TRC') in order to invest in India and to avail the benefits under the DTAC. This

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31 Monika Aggrawal, *Case Study: Regulatory Failure to Re-negotiate India-Mauritius Tax Treaty*, 4(6) IJM P. 01- 06(2013), *available at:*http://www.iaeme.com/MasterAdmin/UploadFolder/10120130406001-2%5C10120130406001-2.pdf, (last visited Aug. 04, 2020).

32 Aswath Rau and Pallabi Ghosal, *Entering the Tiger's Den: Foreign Investment in India through Mauritius or Singapore,* SINGAPORE LAW GAZETTE (2012).

33 *Vodafone International Holdings B.V.* v. *Union of India* (2012) 341 S.C.C. 1, para 197.

finding is stated in various reports which point out round tripping of money in the form of FDI and FII[34].

India and Mauritius entered into Memorandum of Understanding (hereinafter referred as 'MOU') in 2002.The said MOU was for exchanging the information between the Mauritius Financial Services Commission and the Securities Exchange Board of India (hereinafter referred as 'SEBI')[35]. Mauritius Government have also tightened the norms of issuance of TRC's by enacting more stringent Know Your Client (KYC) regulations and anti-money laundering laws.[36]

A possible solution to the problem of Round Tripping can be that only those companies which are registered and recognized by the stock exchanges must be given permission to avail the exemption for its capital gains under the Treaty. The said company should have a total expense of SGD 200,000 or more on operation in Mauritius for at least two years prior to the capital gain arising.[37]

The Indo-Singapore DTAC which is similar in nature to the Indo-Mauritius DTAC, provided for exemption of capital gains. However, India and Singapore entered into an agreement in 2005 to this effect. It still provides for the exemption but in 2005 a restriction clause was incorporated which stated that the company must have an expense of more than $200,000 in preceding years to avail the benefits of DTAC.[38]

Another possible solution is to insert a special anti-treaty shopping clause in DTAC which is present under Article 24 of the Indo-USA DTAC.[39] The presence of such a clause will make it very difficult for the contracting states to prohibit the residents of the third country from availing the benefits of the DTAC.

India, like Indonesia, can even decide to terminate the DTAC entered with Mauritius. However, such a step might have serious repercussions as most of investments flown to India are through Mauritius route.[40] Therefore, in devising a route out to enhance tax revenue from such transactions, India must take a holistic and pragmatic approach.

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34 T.C.A. Ramanujam, *The Vodafone saga and FDI*, THE HINDU BUSINESSLINE (Mar. 07, 2017) *available at*:http://www.thehindubusinessline.com/industry-and-economy/taxation-and-accounts/article2885982.ece (last visited Aug. 04, 2017).

35 Aayush Kumarand Varun Natarajan, *Indo-Mauritius DTAA: The Way Forward* in INTERTAX (2013).

36 *Id.*

37 Nishith Desaiand Dhruv Sanghavi, *The Travails of the Indian Mauritius Tax Treaty & The Road Ahead*, (2008).

38 *See*, Article 3, Protocol Amending the Indo- Singapore DTAC.

39 *See*, Article 24, *Limitation on benefits*, Indo-US DTAC.

40 *Supra*, note 34.

Transfer Pricing

When unrelated parties, doing similar business, agree to a price in the open market, such an agreement is known as *Transfer Pricing*.[41] Transfer price is important to both the taxpayers and authorities as it determines large parts of income and expenses and taxable profits under different tax jurisdictions.[42]The real issue under transfer pricing is that the price which is determined to be exchanged between the contracting parties is exchanged in some other country. This affects the economy of the State where the parties are doing business.[43]

The problem of Transfer Pricing can be resolved if India enter into Advance Pricing Agreement Program (hereinafter referred as 'APA') which has been introduced by the Finance Act, 2012. This program has already been announced byCBDT.[44] Under this agreement a person who is entering into atransaction shall be eligible to make APA. The person who has entered such APA must file the income return of that year within 30 days.APA could stabilize the atmosphere for tax payers in these transfer pricing matters. APA's are consideredto reduce the litigation expenses and avoid the risk of double taxation. Certainty can be seen in the regulatory framework of the companies too.

Information Sharing

Exchange of information between the countries which enter into DTAC is inevitable as also necessary for effective taxation of the e-commerce entities. Article 26 of Indo-Mauritius Agreement provides for the exchange of information with respect to the taxes. However, the extent to which the information is exchanged can be limited by the countries. India's DTAC agreements with other countries provide for the exchange of the information. On comparison of Article 26[45] of the Indo-Mauritius DTAC with the OECD Model, it is clear that scope of Article 26 is very limited as it gives out the discretion to both countries on extent of

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41 OECD, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*, *available at*:http://www.oecd-ilibrary.org/taxation/oecd-transfer-pricing-guidelines-for-multinational-enterprises-and-tax-administrations_20769717(last visited, Jan. 22, 2020).

42 *Id*.

43 Roy Rohatgi, BASIC INTERNATIONAL TAXATION 412-427 (2005).

44 CBDT, *Notification No. 36 of 2012* (2012), *available at*: http://www.incometaxindia.gov.in/booklets%20%20pamphlets/advance-pricing-agreement-guidance-with-faqs-(tpi-43).pdf; *see also*, http://www.itatonline.org/info/?dl_id=1011(last visited Feb. 08, 2020).

45 *See*, Article 26, *Exchange of Information or Document*, Indo-Mauritius DTAC.

sharing the information.[46] The OECD Model Tax Convention Article 26 dealing with sharing of information which on the other end is wider in its ambit.[47]

The MOU signed between India and Mauritius, states that the tax authorities of both the countries can help each other in order to find the misuse of the Treaty like insider dealing and manipulation in securities and other dealings. The objective of the MOU is for development of markets in both countries through best practices. Different norms are laid down in order to check the misuse of the treaty. The main aim of the MOU is to find the transactions which were maliciously made in order to evade taxation. Mauritius has also implemented KYC and has taken steps to further anti-money laundering measures to stop the misuse of the treaty.[48]

It is suggested, that India must enter into a Tax Information Exchange Agreement (hereinafter referred as 'TIEA') with Mauritius. India has entered into similar TIEAs with almost nine countries like Bermuda; Cayman Islands etc.[49] Entering into a TIEA will enable both countries to effectively exchange information. The TIEA's concluded by India with certain countries are based on OECD convention. The OECD commentary on model agreement points that exchange of Information is for the widest range and extent.[50] Article 3 of the Agreement between the Government of the Republic of India and the Government of the Cayman Islands is pertinent here. It deals with the Exchange of Information with respect to taxes and covers the list of taxes under which exchange of information can be done. However, the TIEA's concluded by India covers every kind of tax.[51] India must enter into such kind of TIEA with Mauritius which can help in collecting the right information. Such TIEA must be in accordance to the OECD standards which are actually beneficial for India.

General Anti-Avoidance Rules (GAAR): Whether a Possible Solution?

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[46] *Supra*, note 37.

[47] *Id*.

[48] NDTV, *India- Mauritius Agree to Negotiate on Double Taxation Issue*, *available at:* http://www.ndtv.com/india-news/india-mauritius-agree-to-negotiate-on-double-taxation-issue-745978(last visited Feb. 18, 2020).

[49] *See*, *DTAC Entered with Countries*, *available at:*http://law.incometaxindia.gov.in/DIT/intDtaaTIEA.aspx(last visited Aug. 10, 2017).

[50] *See*, *Agreement on Exchange of Information in tax matters*, available at – http://www.oecd.org/ctp/harmful/2082215.pdf(last visited Aug. 04, 2020).

[51] *See*, Article 3, *Agreement between the Government of the Republic of India and the Government of the Cayman Islands for the Exchange of Information with Respect to Taxes*, *available at:*http://tia.gov.ky/pdf/Agreement_-_India_-_21_March_2011.pdf(last visited Dec. 20, 2019).

Procedures to counter tax avoidance, such as, Targeted Anti Avoidance Rules (hereinafter referred as 'TAAR') or Specific Anti Avoidance Rules (hereinafter referred as 'SAAR') have already been in force for long. Therefore, the idea of giving place to anti avoidance rules in tax legislation is not novel to India at all. The IT Act under Chapter X provides for 'special provisions relating to avoidance of tax'.[52] It already provides for anti-avoidance rules relating to transfer pricing,[53] transactions with non-residents[54], securities transactions[55] etc. Apart from these statutory provisions the judiciary has also played a role in developing anti-avoidance rules.[56] However it was felt that these SAAR cannot combat the more creative forms of tax avoidance that employ transactions that tax authorities cannot predict. Thus, the Direct Taxes Code bill introduced General Anti Avoidance Rules (hereinafter referred as 'GAAR').[57]

GAAR is a principle-based rule within the country's tax legislation for avoidance of tax. It is a mechanism which provides the tax authorities to deny the tax benefits on transactions which don't have any commercial justification but are only entered to avail tax benefits.

GAAR was initially proposed to be introduced in India in *Direct Taxes Code, 2009*.However; it came before the parliament through Direct Taxes Code, 2010. Later Chapter X-A was introduced in the Act through Finance Act of 2012 which incorporated the detailed provisions of the GAAR. This incorporation created havoc worldwide as it was targeting the transactions of Indo-Mauritius DTAC.[58]The main concerns of the investors with that the introduction of GAAR were:

- Should not end up penalizing tax-payers, who have genuine reasons for entering into bona-fide transaction.[59]
- The proposals should not lead to any fiscal uncertainty or ambiguity.[60]
- Should be ensured that any of the proposals does not pave the way for avoidable litigation, which is already at a very high level in tax matters.[61]

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52 Tarun Jain, *GAAR' and 'Rule of Law': Mutually Incompatible?* ,43 Chartered Accountant Practice Journal (2013)*available at:*http://ssrn.com/abstract=2298520(last visited Dec. 20, 2019).

53 *See*, section 92 to 92F, Income Tax Act, 1961.

54 *Id.* section 93.

55 *Id.*section 94.

56 *Vodafone International Holdings* v. *Union of India* (2012) 341 I.T.R. 1, para 183.

57 *Supra*, note 50.

58 U.P. Singh, *The Folly Continues: GAAR- A Critical Analysis*, , 11(2), Journal International Taxation(JIT) 503 (2014).

59 *Supra*, note 51.

60 *Id.*

61 *Supra*, note 55.

In order to address the above issues, the then Prime-Minister who was also holding the Finance portfolio constituted a committee headed by Dr. Parthsarthi Shome and the Committee submitted the key recommendations under the existing GAAR provisions:[62]

1. The Implementation of GAAR should be deferred for 3 years
2. Abolish the capital gains on transfer of the listed securities for both residents and non-residents.
3. Constitution of high powered 'Approving Panel'
4. Tax mitigation to be distinguished from tax avoidance before invoking GAAR and that it should be applied in case of artificial arrangements
5. A monetary threshold of Rs.3crore of tax benefit to a tax payer in a year should be used for the applicability of GAAR provisions

In accordance with the recommendations made by the committee Chapter X-A was amended through Finance Act, 2013 and it was stated that GAAR will be effective from 1st of April, 2016. Again the implementation of GAAR was deferred in the financial budget of 2015-2016 and it shall be come into force from April 01, 2017.[63]

The CBDT has recently notified rules[64] that would govern India's new GAAR Provisions. The rules are meant to introduce certain safeguards but there are still certain ambiguities prevailing over such rules such as lack of commercial substance, substantial commercial purpose, bona fide objects, abuse and misuse of law.[65] The major concern of the investors is that GAAR gives the tax authorities too much discretionary power to determine whether a particular transaction has commercial justification or not. It is believed that the use of GAAR provisions will be used as a weapon to intimidate taxpayers.[66]

It is believed that through the introduction of GAAR provisions, there shall be a check on the transactions of the investor and this would ensure that there is no treaty shopping and round tripping. Another advantage is that the tax authorities are given a free hand to determine the arrangements between the parties in order to find out the whether the transaction is actually for tax benefits through various means. GAAR necessarily can be used by the Government as necessary anti-avoidance measures in order to prevent the investors from taking undue benefit of the DTAC by E-Commerce enterprises.

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62 *Supra*, note 52.

63 Remya Nair, *Budget brings clarity on GAAR for Investors,* THE LIVEMINT (2015), *available at*: http://www.livemint.com/Politics/6IP8PO6wHsvQe7FkjFaruK/GAAR-deferred-by-two-years.html(last visited Feb. 20, 2019).

64 *See*, section 95, Applicability of GAAR, The Income Tax Act, 1961 (Act No. 43 of 1961).

65 Nishith Desai, *Indian GAAR: Rules Notified- Some Relief, But Ambiguities Remain* (2013).

66 *Id*.

VII

Conclusion

The environment that surrounds us is dynamic. The method of transacting business has also undergone lot of changes in a last decade. We have taken a step further, from conventional form to using internet as a medium for exchange. Since the beginning of digital age, regulation of the E-Commerce has been a challenging task. Levying taxes on E-Commerce entitiesis a tedious process. Various legislation for instance The Income Tax Act,1961 lays down the provisions, that tax the E-Commerce entities based on the business connection and their status. Identification of the server in case of such E-Commerce entities becomes necessary for accurate identification of their location. A separate legislation or a statute should be prepared for regulating these E-Commerce entities.

Various conventions like the OECD and Ottawa Conventions have dealt with the problem of regulating these entities. However, if any difficulty arises one has to take the recourse to Courts. And Courts decide each matter on the basis of respective merits. The judicial pronouncements too differ from each other as 'There is subjectivity involved in Interpretation of provisions' by the Judges. The ambiguity existing in the provisions of The Income Tax Act and other legisla tions are also important and need to be plugged for effective e-commerce taxation. E-Commerce is not only regulated by the Income Tax provisions, but it also attracts the Customs or Excise Tax legislations.

'Tax Havens' poses yet another problem. Mauritius is considered as one of the 'Tax Haven' for India. These entities invest in India through Mauritius which gives rise to other problems such as Round Tripping, Transfer Pricing as well as Exchange of Information. A way to overcome this problem can be to amend the existing provisions of the DTAC.

Considering, *Article 13 of the DTAC*, Capital gains should be taxed keeping in mind the 'situs', that is, from where the source of income is been derived and not solely on the basis of the residential status of the investor. Such an amendment can be made to overcome the problem of TRC and control of the company. For instance, if there is sale of shares of an Indian Company, then the profits derived from such a sale will be taxable in India, since source of income is in India. Such an amendment was brought to the India-UAE DTAC which took away the Capital gain Protection.

Similarly, *Article 4 of the DTAC* which defines Residents as a person liable to be taxed on the reason of his domicile, residence, place of management and other criteria of similar nature should be amended. Apart from the aforesaid conditions,

it should also amend the place of actual control and management of the Mauritian company. It should be in Mauritius. Such amendment will substantially dilute the misuse of treaty, if it is revealed that the Mauritian company's actual control and management is not in Mauritius. The author has not provided the exhaustive list of amendments that can be made. Hence, concluding that regulating the E-Commerce is not impossible. Various loopholes in the legislations and their provisions can be filled through amendments in the same.