# TAXATION OF THE DIGITAL ECONOMY IN INDIA - CHALLENGES OF E-COMMERCE AND OTT PLATFORMS

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**ABSTRACT**

India's tax system was not designed for a world where companies can earn crores from Indian user without having any physical presence in the country. For example, e-commerce platforms such as Amazon and Flipkart, as well as OTT (Over the Top) streaming services like Netflix and Amazon Prime Video, generate substantial revenues from Indian consumers, but many do not pay the full amount of tax that would typically be incurred in accordance with Indian tax law. This is largely due to India's tax laws and international tax treaties being created around the concept of establishing a permanent establishment. In other words, they do not consider a company operating in India to be "taxed" unless there is a physical business location or presence of the organization in the country. This paper examines the efforts of the Government of India to provide solutions to this dilemma by way of implementing new tax legislation as well as identifying what else will be needed to ultimately resolve this issue.

India has taken several steps to address these gaps, including the Equalisation Levy introduced in 2016 and expanded in 2020 and abolished by April 2025, and the SEP doctrine, Section 19-OTDS and the OIDR-GST framework. However, each of these measures has its own limits and problem. The Equalisation Levy created double taxation and was ultimately repealed; the SEP doctrine cannot be applied due to the existence of India's tax treaties; and the OIDAR-GST framework is suitable only for indirect taxes and does not address the direct taxation void created by new digital business models. This paper ends with five recommendations, including renegotiating India's tax treaties, introducing a new creditable digital service tax, and preparing for OECD pillar one.

**Keywords:** Digital Economy, E-Commerce, OTT Platforms, Equalizations Levy, SEP, OIDAR, Permanent Establishment, GST, BEPS, Income Tax Act 1961.

## INTRODUCTION

Today, a large part of business happens online. People shop on Amazon, watch Netflix, and use Spotify, all from their phones without stepping into any physical store. These online companies provide their products and services over the internet and charge their Indian customers, but they do not have a physical presence (office, employee) in India. To determine whether a foreign company can be subject to taxation in India, Indian tax law employs the idea of Permanent Establishment. A company that does not have an office or branch in India typically will not be liable for Indian taxation even though it earns crores of rupees from Indian users. The digital economy of India accounted for 11.74 percent of GDP during FY 2022-23 and will be expected to reach 20 percent by FY 2029-30. The e-commerce industry is expected to generate $325 billion by 2030, and the OTT industry generates over 20,000 crore (approximately USD 2.55 billion) in revenue annually in India however, much of that income escapes taxation in India.

India attempted to address this issue by implementing the Equalisation Levy in 2016 and 2020, Significant economic presence (SEP) rules in 2018, Section 194-O[1] TDS on e-commerce in 2020, and the enhanced OIDAR-GST framework in 2023-24. This paper looks at how laws work, where they fall short, and what India should do next.

## REVIEW OF LITERATURE

### i. The OECD's BEPS (Action Plan 1 Report, 2015)[2]

The work confirmed that PE-based tax rules are structurally inadequate for digital businesses. It identified three core challenges of nexus, data valuation, and characterisation and proposed the equalisation levy, withholding taxes, and SEP as remedies, all of which India adopted.

### ii. Lucas-Mas and Junquera-Varela (World Bank, 2021)[3]

This paper argued that only a multilateral treaty-based solution can create a stable digital tax framework, as unilateral measures create double taxation and trade disputes. This

[1] Finance Act, 2020, § 194-O (India).
[2] OECD, Addressing the Tax Challenges of the Digital Economy, Action 1 Final Report (2015).
[3] C.O. Lucas-Mas & R.F. Junquera-Varela, Tax Theory Applied to the Digital Economy (World Bank 2021).

supports India's need to engage with OECD Pillar One.

**iii. Forget Mpofu (Economies MDPI, 2022)[4]**

The work**,** founds that unilateral digital service taxes generate some revenue but cause double taxation and bilateral trade friction, directly mirroring India's Equalisation Levy experience.

**iv. Sarvamangala and Farzana A. (SJCC Management Research Review, 2022)[5]**

This paper argued that the Equalisation Levy reduced the tax gap between domestic and foreign digital firms but suffered from definitional ambiguity and double taxation risk due to treaty incompatibility.

**v. Dr. Jyotirmoy Koley (IJRIAS, 2025)[6]**

This work gives, India's combined measures which represent significant reform, treaty override and profit attribution challenges continue to limit practical effectiveness against large foreign platforms.

**vi. Nayyar and Singh (Indian Journal of Finance, 2018)[7]**

This paper identified the OIDAR provision as India's first meaningful effort to capture foreign digital service providers under indirect tax but noted weak enforcement in B2C transactions. Research Gap Most existing literature analyses the Equalisation Levy or the OIDAR framework separately. No existing study brings together the full abolition of the Equalisation Levy by April 2025 and the updated OIDAR rules specifically for OTT platforms. This paper tries to address that gap.

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[4] Forget Y. Mpofu, Taxation of the Digital Economy and Direct Digital Service Taxes, 10 ECONOMIES 219 (2022).

[5] R. Sarvamangala & Farzana A., A Comprehensive Analysis of Digital Taxation in India, 11 SJCC MGMT. RES. REV. (2022).

[6] Jyotirmoy Koley, Taxation in India's Digital Economy: Challenges, Reforms, and Global Alignment, X IJRIAS (2025).

[7] A. Nayyar & I. Singh, A Comprehensive Analysis of Goods and Services Tax in India, 12 INDIAN J. FIN. (2018).

## RESEARCH METHODOLOGY

Using a doctrinal research method, this paper analyses India's existing tax law as it relates to taxing digital business. Doctrinal research consists of reading statutes, regulations, notices and judgments in order to understand the law as it is stated, in order to make some conclusions about how the law works. This is the most frequently used research method in law because the primary purpose is to analyze the law itself rather than to collect data from individuals using surveys and interviews. The doctrinal approach is appropriate for this purpose because the primary research question is whether the existing tax laws in India are sufficient to tax digital businesses.

The primary sources used in this paper includes the Income Tax Act, 1961[8], Finance Acts from 2016-2025, the CGST Act 2017, the IGST Act 2017, CBDT notification and circulars, and judicial decision from ITATs and the Supreme court of India accessed from Indian kanoon, SCC online and Manupatra. The Integrated Goods and Services Tax Act (2017), notifications and circulars that have been issued by the CBDT, judicial decisions issued by the Income Tax Appellate Tribunal, and decisions from the Supreme Court of India. The appropriate method of study for this issue is to do doctrinal research as it relates to a legal and structural issue. The issue is not the question of how many individuals pay taxes, but instead is the question of whether the law allows for a proper taxation of digital enterprises by the nation of India. By analyzing statutes and court decision, this paper identifies what the laws currently allows, where it falls short, and what changes are needed.

## Chapter 1: The Concept and the scope of the digital economy in India.

### 1.1 Meaning of the Digital Economy.

The digital economy refers to all economic activity that takes place through the internet and the digital technology. This includes buying and selling goods, online streaming content, placing digital ads, using cloud storage, and playing online games. The key difference between a traditional economy and the digital economy is that companies do not have to have any physical presence within a country in order to earn revenue from users in that country, as companies have no need for an office, factory, or employee base located in

[8] Income Tax Act, 1961, No. 43 of 1961 (India).

India to earn thousands of crores of rupees from Indian consumers. The OECD[9] defines this characteristic as the ability of digital businesses to operate independently or mostly independently of the physical assets needed to create & generate economic value. These old tax rules were bult on the idea that if a company is doing business somewhere, it must have a physical presence there. Traditional tax law was predicated on the belief that if an organization was engaging in business at a particular location, they must have a physical footprint there.

The permanent establishment rule was established as a result of this logic and has formed the basis of international taxation for decades. However, digital businesses break this assumption completely. They create their services in one country, house their servers in another country, process their payments in another country, and give their services to users in yet another country, without creating a taxable presence in the location where they are making their profits. Therefore, a foreign OTT platform or e- commerce company can earn billions from Indian user and pay almost no tax in India and this is completely legal under the current rules.

**1.2 Scale of the Digital Economy in India.**

India's digital economy is one of the largest and the fastest- growing in the world. In FY 2022-23, the digital economy[10] produced 11.74% of India's total GDP of INR 31.64 lakh crores (about USD 402 billion) according to the MeitY and ICRIER State of the Digital Economy Report[11]. This contribution should rise to approximately 20% by FY 2029-30, which means that India's digital economy is growing larger than agriculture and manufacturing sectors relative to their other respective industries. Moreover, India processed 1,644 billion UPI (Unified Payment Interface) transactions in FY 2023-24, which is more UPI transaction volume than any other nation worldwide. The expectation for India's e-commerce market to generate revenues around USD 325 billion by 2030 is also evident in the sudden increase of OTT video streaming platforms generating revenues over INR 20,000 crore per year to Indian users.

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[9] OECD, Addressing the Tax Challenges of the Digital Economy, Action 1 Final Report (2015).
[10] Ministry of Electronics & Information Technology & ICRIER, *State of India's Digital Economy Report 2024* (2024) (India).
[11] Ministry of Electronics & Information Technology & ICRIER, State of India's Digital Economy Report 2024 (2024) (India).

### 1.3 Categories of the Digital Economy.

These numbers show 2 things: how much values the digital economy creates in India, and how much tax revenue is losing because foreign digital companies do not pay their fair share. If an Indian digital business were to produce the same amount of revenue from Indian customers, they would pay 25.17% income tax rate on their profits. In contrast, many of the foreign digital businesses earn the same amount of revenue from Indian consumers would pay virtually no income taxes to the Government of India because they have no permanent establishment operating within India as well as being protected by the income tax treaty between their home country and India. This puts Indian digital companies at a disadvantage since they pay full taxes while foreign competitor doing the same work pay very little. For tax purpose, India's digital economy can be split into 3 groups one, the e-commerce platforms like Amazon, Flipkart & Meesho that connects buyers and seller, second the OTT and content platform like Netflix, Amazon prime video & Spotify and the third the other digital services like cloud computing and online gaming. The focus of this paper will be on e-commerce and OTT content because these categories contain many of the most important for tax purposes and have more Indian users than any other segment and are receiving the largest amounts of money from foreign companies.

## Chapter 2: E-commerce platforms taxed under Indian tax laws.

### 2.1 The permanent Establishment Problem.

Section 9(1)(i) of the Income Tax Act 1961[12] serves as the basis for determining e-commerce taxation in India. Under this provision, income is taxable in India if it arises through a business connection in India. However, if a foreign taxpayer is resident in a country with a Double Taxation Avoidance Agreement ('DTAA') with India, the provisions of the DTAA will apply instead of the provisions of the Income Tax Act. DTAAs will typically follow the OECD or UN Model Convention, which limits India's ability to tax business profits earned by a foreign corporation to those cases where the foreign corporation has a Permanent Establishment ('PE') in India. A PE is defined as having a fixed place of business (i.e., an office, factory, etc.) through which the business carries out all or part of its activities. For example, a foreign e-commerce platform that operates

[12] Income Tax Act, 1961, § 9(1)(i) (India).

entirely online and has no physical presence in India will find it extremely difficult to establish that it has a PE in India. Companies such as Amazon that route their operations through US and Irish entities and the large Chinese e-commerce platforms that operate through Singapore-based structures currently have no fixed place of business in India which meets the physical presence test of establishing a PE as required by Indian income tax law.

### 2.2 ITO v. Right Florist Pvt. LTD 2013.

The issue here was clarified by the ITAT Kolkata in its foundational case being, *ITO v. Right Florists Pvt. Ltd.,* 2013[13]. A florist located within the Indian sub-continent paid RS 30.44 Lakhs to Google Ireland and Yahoo[14] USA for 'advertising services' provided electronically. The Income Tax Officer contended that the florist in question was required under section 195 of the Income Tax Act (ITA)[15] to withhold TDS prior to making these payments, which the Tribunal found to be completely unmeritorious since the conduct of either Google or Yahoo in providing their services to the florist was not in India (i.e., there was no permanent establishment (PE) in India of either Yahoo or Google since their respective servers were each located outside India). The payment was not royalty under Section 9 (1) clause vi of ITA because the florist was not using any copyright of Google or Yahoo. they were also no fees for technical services under section 9(1)(vi) because the services were fully automated with no human technical input. The income was therefore pure business profit of companies without an Indian PE, and India had no proper to tax it. Right Florists became the most important precedent in India's digital tax law and directly triggered the legislative changes that followed.

### 2.3 Significant Economic Presence Section 194-O.

The Finance Act 2018 added Explanation 2A to Section 9 (1) (vi)[16] of the Income Tax Act[17] to implement the concept of having a significant economic presence (SEP) in India by way of income or business connection for non-residents A non-resident who has a business connection in India if he either earns more than INR 2 crores from Indian transaction in a year or engages with more than 3 lakhs Indian users through digital means in a year. India

[13] ITO v. Right Florists Pvt. Ltd., (2013) 25 ITR (T) 639 (ITAT Kolkata) (India).
[14] Yahoo India Pvt. Ltd. v. DCIT, (2011) 140 TTJ 195 (ITAT Mumbai) (India).
[15] Income Tax Act, 1961, No. 43 of 1961 (India).
[16] Income Tax Act, 1961, Explanation 2A to § 9(1)(i) (India).
[17] Income Tax Act, 1961, § 9(1)(vi) (India).

will consider all above-mentioned income as part of the SEP, along with any advertising income received for targeting Indian residents, data received from Indian users and sold to others, and the sale of merchandise as well as the provision of services based purely upon data collected from Indian users. However, the SEP rules have one major limitation. India's tax still uses the old PE definition, so a foreign company from a treaty country can simply invoke its DTAA and override the SEP rule, removing any income tax liability in India.

## Chapter 3: The major challenges in taxing OTT platforms in India.

### 3.1 Business Model and Direct Tax Gap.

The SEP rules currently work only against companies that have no tax treaty with India, which is a very small group. Section 194-O[18] introduced by the finance Act 2020, requires e -commerce operator like Amazon & Flipkart to deduct 1%TDS from the payment made to resident individual seller whose annual sale exceeds INR 5 lakhs. Similarly, *Section 52*[19] *of CGST Act 2017*[20] requires a 1% TCS obligation from the e-commerce operator on all supplies made through the available e-commerce platform. Recent clarification from the CBDT through Circular 20 of 2023 addressed issues regarding TDS or TCS applications in scenarios involving multiple operator ONDC-based transactions. These provisions will clearly assist small sellers; however, they do not resolve the issue concerning the income attributable to foreign-based e-commerce platform operators.

### 3.2 The OIDAR framework under GST.

India's best current tool for taxing foreign OTT companies is OIDAR framework under section 2(17)[21] of the IGST Act 2017. According to the definition, OIDAR services include any service that is provided using technology via the Internet, including the streaming of motion pictures, television shows and music, online gaming, digital storage, and distance education. If a company provides an OIDAR service to an individual who resides in India, then the location of supply would be deemed to be in India so the service would be subject to the Goods and Services Tax (GST) at a rate of 18%. The foreign supplier must register for GST in India using form GST REG-10, and must also submit monthly returns using

[18] Finance Act, 2020, § 194-O (India).
[19] Central Goods and Services Tax Act, 2017, § 52 (India).
[20] Central Goods and Services Tax Act, 2017, §§ 24(ix), 52 (India).
[21] Integrated Goods and Services Tax Act, 2017, No. 13 of 2017, § 2(17) (India).

form GSTR-5A along with making an 18% IGST payment for all sales of subscriptions.

The Finance Act 2023–24 made a major amendment to the OIDAR definition by deleting the words essentially automated and having minimal human input.15 A foreign OTT service would previously have been able to argue that the content it supplied, such as an original Netflix series created by real directors or writers or actors, was not essentially automated and therefore not covered by the OIDAR definition. The 2023–24 amendment eliminated this argument by changing the definition of OIDAR to focus on the manner in which the service was provided over the internet rather than how much automation went into creating the content. Following these amendments, the CBIC issued compliance notices to about 70 different foreign digital service providers in October 2023 instructing them to register for GST. Many of the largest providers, including Netflix and Spotify, have now been registered and are remitting 18% IGST on Indian subscriptions, which has materially improved the coverage of the Indian indirect tax system for the OTT industry.

### 3.3 Characterization: are Subscription Fees Royalty.

There is also another issue regarding how subscription fees for OTT platforms will be treated for purposes of direct taxation. If subscription fees qualify as royalties within the meaning of Section 9(1)(vi) of the Indian Income Tax Act[22] ("ITA"), India would have the ability to impose withholding taxes on foreign sources of OTT income (without requiring a permanent establishment) at the applicable tax treaty withholding rates (generally between 10 and 20 percent). This would increase the ability of the Indian government to assert taxing jurisdiction over income derived from entertainment produced by foreign OTT providers. The Revenue has a reasonable basis to believe that OTT subscription fees are royalties because OTT subscribers pay to gain access to copyrighted music and films something for which copyright would be considered to be granted. The Supreme Court also provided guidance in the case *Engineering Analysis Centre of Excellence Pvt. Ltd. v CIT*[23] (2021). The Court's decision determined that there is no royalty involved with respect to payments for licenses allowing the end user to use a software copy since there is no copyright or right of exploitation that transfers to the end user. Instead, the end user receives a personal license to only one copy of the software product. In similar fashion, an OTT

[22] Income Tax Act, 1961, § 9(1)(vi) (India).
[23] Engineering Analysis Ctr. of Excellence Pvt. Ltd. v. Comm'r of Income Tax, (2021) 432 ITR 471 (SC) (India).

subscriber will only receive a personal nontransferable license to view films or series; the subscriber will not obtain any copyright to those films or series through the subscription. Therefore, OTT subscription fees should not be treated as a royalty. The ITAT Bengaluru also considered the legal treatment of OTT subscription fees and came to a very different conclusion in *Google India Pvt. Ltd. v. ACIT* (2018)[24]. In that case, the ITAT characterized payments made pursuant to the AdWords agreement as royalties based on the conclusion that advertisers are being provided access to patented technology through the use of the AdWords agreement. These conflicting decision show that court still disagree on how to classify digital payment. Since no Indian Court has directly decided the OTT royalty question, both tax department and foreign platform face real legal uncertainty.

### 3.4 Enforcement Difficulties.

Enforcing a clear legal obligation under OIDAR-GST is challenging when targeting foreign OTT companies. A foreign OTT companies with no employees, bank accounts, or property in India cannot easily be forced to comply. India also has no tax collection agreement with major OTT home countries like Netherlands, Luxemburg, Sweden & Ireland. Currently compliance is generally dependent on voluntary compliance from large origin brands (ex: Netflix, Spotify) who have incentives to register for GST purposes in order to protect their reputation and maintain access to the Indian market. On the other hand, compliance from smaller foreign digital platforms is routinely ignored with limited short-term repercussions. A more systemic enforcement approach would be implementing withholding and remittance obligations for digital payment intermediaries for examples UPI processors, banks and credit card companies, and app stores like Google Play and Apple App Store) with respect to applicable IGST on subscription fees owed by foreign OIDAR companies before remitting subscription fees to the foreign OIDAR companies. This would create an automated compliance mechanism thereby eliminating any requirement for voluntary compliance by the foreign platform similar to the EU's One Stop Shop VAT mechanism for digital services.

## CONCLUSION

India has tried hard to tax digital economy through the Equalization Levy, the SEP rules,

[24] Google India Pvt. Ltd. v. ACIT, ITA No. 2845/Bang/2017 (ITAT Bengaluru 2018) (India).

Section 194-O and the OIDAR framework. But none these measures have fully worked when it comes to taxing the actual profit of large foreign digital platforms. The Equalization Levy, will no longer exist after April 2025, and therefore India will not have any direct way to tax profit that foreign companies earn from use of their digital platforms. The SEP Rule is blocked from use because of India's tax treaties that almost all major foreign digital platforms have in place. The rules in Section 194-O and TCS under CGST apply to small Indian sellers but do not apply to the income earned via foreign providers. The OIDAR-GST framework is currently the most applicable law available to tax digital platforms, especially after the 2023-24 amendments have become law however, the OIDAR-GST framework merely applies to indirect taxation. Judgments rendered vary from the 2013 judgment of the ITAT Kolkata in Right florist, to the 2018 ruling of the Income Tax Appellate Tribunal in Google India, and finally to the Supreme Court ruling in Engineering Analysis in 2021, which each determine whether a digital payment is to be taxed. Inconsistency in the courts creates additional uncertainty and risk of litigation for everyone concerned.

There are five recommendations made for India's tax issues. First, India needs to renegotiate its tax treaties with the USA, Ireland, the Netherlands, Luxemburg, Sweden, and Singapore to include a SEP nexus rule in the tax treaties so that the SEP rule can be enforced without having to go through a domestic law enforcement process. Second, a new digital services tax should be structured as an income tax under the treaty law so that foreign businesses can credit it in their home countries instead of being subjected to double taxation as a result of repealing the EL. Third, legally enforce payment processors, UPI operators, and app stores to withhold taxes and remit GST of all payments made to foreign OIDAR companies before transferring funds, so the collection of the tax is automatic. Fourth, provide small online sellers with a simplified tax option for presumptive taxes to minimize the compliance burden caused by Section 194-O and GST TCS. Fifth, India should start preparing its domestic law to comply with the OECD Pillar One framework so India can have an entitlement to treaty-revenue-sharing for all global firms regardless of their PE. In the end, taxing the digital economy is about fairness, making sure that the values created by India’s internet user also benefits India’s School, hospitals & public services.