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IMPACT OF TAX ON E-COMMERCE IN REFERENCE TO STARTUP: A CRITICAL STUDY WITH ENTREPRENEURSHIP LAWS IN INDIA

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Abstract

The Internet has evolved from a network of computers to a global social phenomenon. Once a medium that offered access only to a few, the smartphone and mobile network revolution has thrown it open to a much wider and more varied audience. In the process it is transforming itself from a place where people exchange information to a place where people conduct business as well. The convenience provided by online business transactions – e-commerce – is the reason why more and more users are turning to the Internet for their buying and selling. This is not only changing the face of retailing and rewriting the rules of the game but also throwing up new challenges to the legal, policy- making and taxation fraternity at a pace that they are ill-equipped to deal with. This paper presents some of the major conceptual characteristics of e-commerce and the legal and taxation challenges that arise therefrom. It then suggests the approach that could be adopted for tackling these legal and taxation issues.

Keywords: E-commerce, Taxation, Computers, Laws

Introduction

Any business exchange which is done through the internet is known as Electronic business or Electronic Commerce. During recent times, business visionaries, both in India and in foreign countries are considering shifting their businesses to electronic and purchasers are inclining towards these E-Commerce websites for their requirements. The reason behind this is the

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successful results of present ecommerce giants like facebook.com, flipkart.com, amazon.in and many more ecommerce websites which are growing at a very high pace. The business income report which is generated every year of these ecommerce websites is clearly the factor why entrepreneurs these days are considering shifting their businesses to electronic medium.

During nineteenth century, a German jurist, Rudolf Von Ihering, stated: “While the States were fighting one another, trade found out and levelled the roads that lead from one nation to another, and established between them a relation of exchange of goods and ideas.” This statement stated by Ihering in nineteenth century is more applicable in twenty first century. “Transnational activities are expanding at an unprecedented rate and it is expected that this trend will accelerate through the growth of ecommerce and computer networks.”

E-Commerce has been defined by Roger Clarke as “conduct of commerce in goods and services with the assistance of telecommunications and telecommunications- based tools” A.R Lodder defines E-Commerce as “commercial activities concerning goods and services as well as any business, where the participants are not necessarily at the same physical location and therefore do apply communication means”

In the digital age, the conventional methods of transacting business has become extinct as E-Commerce using latest technologies has overcome the transactional manners of transacting business. The E-commerce sector with the help of advance technologies is becoming more reachable and efficient. *Use of computers and Information Technology to transact business by and between entities and individuals is termed as Electronic Commerce.*[5] The markets have transformed from local markets to big shopping malls and now from big shopping malls to online market place where Business to Business (B2B) and Business to Consumer (B2C) transactions are done with the help of payment gateways and online wallets. The simplicity of accessing Information and Communication Technology (ICT) prompted internet based payment methods including net banking, and mobile payments has played a vital role in the development of E-Commerce.

Mobile Commerce – Accelerator of E-Commerce

The International Telecommunication Union in its *Trends in Telecommunications Report 2014* reported that there has been a tremendous growth in the ICT sector, especially in the demand of mobile services and mobile data services, use of 4G, international gateway services and increase of wireless usage in developing countries. The increase in the usage of mobile devices has added to the development of *digital commerce through mobile devices also known as Mobile Commerce or M-Commerce.* In a report by Google it was revealed that 67 percent of digital commerce is performed using mobile devices such as Mobile Phones and Tablets and as many as 40 percent of Google searches in India is performed using mobile devices.

According to a research conducted by PayPal in conjunction with Ipsos in 2015, it is indicated that global *Mobile Commerce growth should outpace Electronic Commerce by 3:1*. There are multiple reasons for the fast growth of M-Commerce as compared to Electronic Commerce. As per the PayPal's report, the escalation in smartphone shopping growth comes from young adults falling within the age of 18-34. Out of all the online shoppers surveyed, about one third of them have assented to the fact that they have used their smartphones for making an online purchase in the past twelve months.

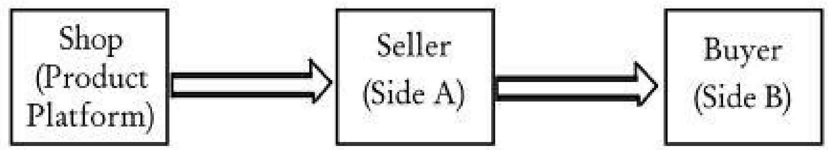
PayPal reports that out of all the smartphones user surveyed, 64 percent users reported using mobile application for making online purchase as compared to the 52 percent users who used mobile browser for the same. There were two main reasons provided by the users for the use of Mobile App i.e. Convenience (by 35 percent users) and Speed (by 30 percent users). Two other major cited by those who were surveyed are Instant Payment Confirmation and having a reminder in the app to use discount vouchers and coupons.

- **PLATFORMS**

A platform is defined as a product, service or system which provides an environment of technologies that permits various kind of users and complementary business partners to interact and benefit from the platform's masked functionality. These business partners are also called complementors.

Traditional companies were engaged in production and selling of products or services. But with the coming of internet and advanced technologies like cloud computing, more and more application ideas are implemented by companies that permits business entities and consumers to interact and transact business. For the better understanding of concept of platform let us examine various types of platforms which are used in virtual space.

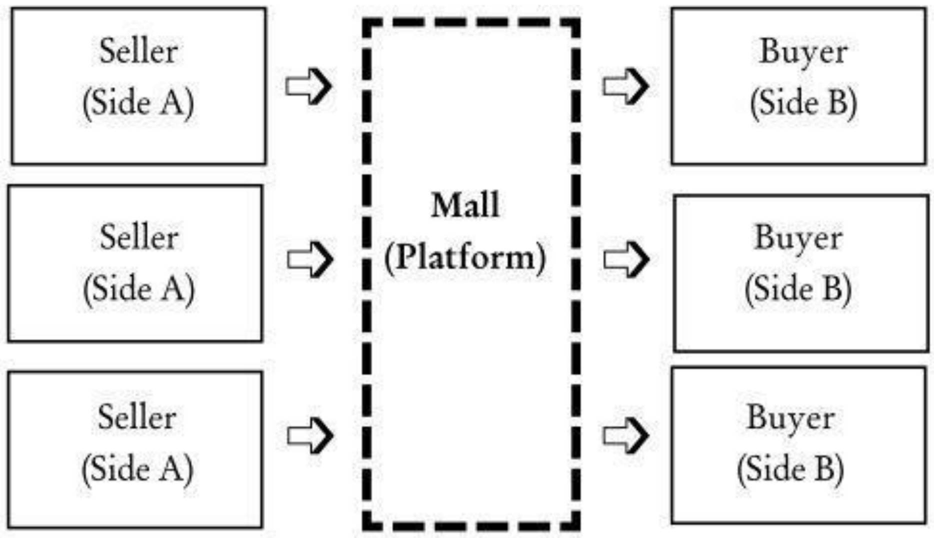
In the physical world, shops provide facility for consumers to purchase goods as shown in the figure:



Here shops are providing a medium to the seller and buyer to conduct business between them. It is a one-is-to-one relationship and therefore traditional shops are said to be ***One-Sided Platform or Product Platform*** i.e. only one party (i.e. buyer) act as customer who transacts with other party (i.e. Seller) while the shop which is providing the platform only acts as facilitator.

Another way of conducting business on this same model is where retailer resells the goods or products manufactured by some other party. It is known as ***Reseller Platform.*** Note that there is only customer in this platform i.e. Side B (Buyer).

Shopping Malls in physical world facilitate the interaction process by providing different type of platform as shown in the figure:



Here mall provide a platform to multiple sellers by renting them space and are therefore customers for the mall. On the other side is the buyer who interact and transacts with sellers of his choice but is not the customer of the platform i.e. mall. Therefore this also one sided transaction because the platform is making money from one side i.e. from seller only.

But that is not the case of Debit/Credit Card Companies like Visa or MasterCard or Games consoles (Gamers and game developers). In this the transaction flow is as follow:

Here VISA provides a medium and facilitate the transaction between merchant and buyer by providing them with a platform for making payments. But in this platform unlike above discussed platform both side have to pay to the Platform for the services it provides, the cardholder pays the card fees and merchant pay the commission on each sale to the platform. This is an example of ***Two Sided Platform.*** Even if the credit card company gives free service (i.e. does not charge any monthly or annual fee from credit card holder) to the cardholder but the holder still has customer relationship with the Company, by consuming the services provided by the company.

Another category of platform is ***Multi-Sided platform***. It provide a medium for different users to interact and transact business that results in multiple revenue stream from multiple players. The illustration of such platform can be Microsoft Windows, where users i.e. buyers can interact and transact with application or software developers (sellers) and hardware suppliers. Multiple players generate multiple revenue stream for platform there it has multiple customers.

- **LAWS ON E-COMMERCE**

There are multiple issues related to cyberspace such as need for high level security in online transactions so that trust of people can be built in order to encourage them to use more online methods of payment. This security can only be provided by an adequate legislative framework to govern E-Commerce. There is an E-Commerce model created by UNCITRAL which forms the basis of many legislations across the world relating to E-Commerce. India also has enacted IT Act, 2000 based on UNCITRAL Model Law of E-Commerce and created a legislative framework that governs not only E-Commerce but also Data Protection and Consumer Protection.

UNCITRAL Model Law on E-Commerce

The Model Law on E-Commerce was adopted on 12 June, 1996 by United Nation Commission on International Trade Law (UNCITRAL). The aim of Model Law on Electronic Commerce (MLEC) is to enable and facilitate electronic commerce by overcoming legal obstacles in international trade through internet. The MLEC was first legislation to adopt the fundamental principles of technological neutrality and non- discrimination. The principle of Technological neutrality ensures that such legislative provisions to be adopted which are neutral with respect to the technology being used. The neutral rule aims at accommodating any future technological development without further legislative framework. The principle of non-discrimination mandates that electronic document would not be denied legal validity or enforceability. The Model law is explained through a guide to enactment. The Guide to Enactment explains that Model Law adopts the functional "equivalent approach" and declares that electronic contracts and electronic documents are as legally valid as paper based contracts.

There are states which have adopted the principles illuminated by MLEC such as India, Mexico, and Australia but there are many states which are not ready to accept that traditional documents or signatures can be replaced by electronic documents or signatures. The UNCITRAL Model Law has setup uniform set of laws on E-Commerce that will continue to guide different legal systems to achieve a regime that adopts technological neutrality, non-discriminatory and functional equivalent approach.

E-Commerce and India's Information Technology Act, 2000

In India, the IT Act, 2000 was enacted to facilitate E-Commerce and grant legal recognition to e-contracting as one of its main objective. The preamble to the IT Act, 2000 read as follows:

*"An Act to provide legal recognition for transactions carried out by means of electronic data interchange and other means of electronic communication, commonly referred to as "**electronic commerce**", which involve the use of alternatives to paper-based methods of communication and storage of information, to facilitate electronic filing of documents with the Government agencies and further to amend the Indian Penal Code, the Indian Evidence Act, 1872, the Bankers' Books Evidence Act, 1891 and the Reserve Bank of India Act, 1934 and for matters connected therewith or incidental thereto."*

The basis of the Indian IT Act is Model Law on Electronic Commerce adopted by United Nation Commission on International Trade Law (UNCITRAL). The provisions of the IT Act which helped facilitating the Ecommerce in India are Section 3 which provides for the authentication of electronic records, Section 4 which provides for legal recognition of the electronic records, Section 5 which provides for the legal recognition of the digital signatures and Section 10 A which validates the contracts formed through electronic means giving validity to click accept methods.

Miscellaneous Laws on E-Commerce in India

Marketing or Retailing in India is controlled by state and central acts which differentiate the multiple shareholders in the supply chain and impose suitable charges on the exchanges or transactions. In 2013, the FDI was allowed by government in multi-brand retail but due to change in government in 2014, there is some ambiguity in this matter. The present position vis-àvis FDI with respect to E-Commerce is contained in ***Consolidated FDI Policy Circular 2016*** which permits 100% FDI in Business to Business (B2B) E-Commerce but no FDI is permitted in Business to Consumer (B2C). But there are few exceptions where FDI in B2C E-Commerce is permitted:

- Where a manufacturer is manufacturing its products in India is permitted to sell through E-Commerce retail. Where a single brand retail trading business is operating through its stores on the grounds is permitted to undertake retail trading through E-Commerce.

Apart from FDI Policy, any other law which would apply to E-Commerce business are:

- The ***Sales Tax Act*** states all sales within a state attract Value Added Tax (VAT) and ***Central Sales Tax, 1956*** is applicable on inter-state sales. Upcoming Goods and Service Tax may supersede the present tax regime.
- The ***Indian Contract Act, 1872*** would apply to ensure valid enforceable arrangement between different stakeholders of an E-Commerce business i.e. buyers, sellers and marketplace platform itself. Because in case of any breach or dispute between seller and marketplace platform, the resolution to the dispute can be determined from the obligations mentioned in the contract between the parties. In addition the ***Specific Relief Act, 1968*** provides the additional remedy of specific performance.
- The laws related to intellectual property such as ***Copyright Act, 1957*** and ***Trademark Act, 1999*** can also be referred in order to determine the intellectual property rights of the stakeholders. For example if any seller is selling fake goods of a very well established brand via marketplace platform due to which there is damage to the reputation of brand, the seller may be sued by the legal brand owner under the said acts.
- The organisation operating an E-Commerce business would also need to fulfil the obligation of applicable local laws such as ***Shops and Establishments Act*** which are different in different states with respect to their physical establishments.
- Further to protect the rights of online consumers, the provisions of ***Consumer Protection Act, 1986 and Sales of Goods Act, 1930*** are also applicable.

- There are some special statutes applicable pertaining to specific goods such as ***Food Safety and Standards Act, 2006*** (for E-Commerce websites such as Box8 and Foodpanda.in) that require specific declarations such as vegetarian/non- vegetarian sign, best before date and nutritional facts amongst other information to made of every packaged food delivered and ***Drugs and Cosmetic Act, 1940***for declarations to be made on products other than food such as medicines delivered online for websites like Apollo.com.
- With respect to B2B business model, the ***Competition Act, 2002*** puts a stop on any anti-competitive agreements, monopolistic and restrictive trade practices that involve abuse of dominant position by a party. It also regulates any kind of combinations of enterprises through mergers or amalgamations of enterprises. This is a general law and will apply in same manner on online businesses too.
- Criminal Liability for any kind of injury or damage caused by any defective product or services being delivered online is imposed by the provisions of ***Indian Penal Code, 1860.*** IPC contains punishment for certain offences such as false weights and measures, false property marks and adulteration of goods apart from the punishment for breach of trust, impersonation and cheating besides other provisions to protect a customer's interest. In order to apply IPC party has to establish beyond reasonable doubt *mensrea* i.e. intention to cause harm and *actusrea* i.e. act to cause injury. This is a general law and will apply in same manner on online businesses too.

- **CONCLUSION**

In present countries have not agreed to adopt and follow a single taxation framework for taxing ecommerce transactions between the countries. A separate legal and taxation framework is following by each country for governing ecommerce in their respective nations. Some states like United States have retail taxation structure, India have VAT (in present and soon going to be replaced by GST) and EU already have GST framework in action. Therefore till now ecommerce taxations are being taxed by amending and extending current tax laws only. There is still a need of evolution of extensive framework for ecommerce transactions.

E-Commerce is changing and growing by branching itself into newer forms. Even M-commerce is expanding at a faster pace than e-commerce. Therefore, not only there is need to strengthen the legal and statutory framework, but also an exhaustive and efficient infrastructure need to assembled to supervise all ecommerce transactions. The skills of the commercial tax department's officer need to be upgraded. Administration need to be improved by educating the consumer of their rights and by increasing the cooperation among different states. Tools and techniques for assisting taxpayers in their dealings with tax department need to be designed. Betterment of authorization controls and audit trails needs to be done. The IT infrastructure needs to be so much efficient that it can cover all transactions among states and even among nations.

Although some of the issues in Current Tax Regime has been addressed by the Model GST Law, but there are still number of issues remaining in the present tax regime that are prevailing. For instance, there has been no provision that how combo offers provided by e-commerce business entity are going to be taxed, another ambiguity is that what will be the amount that is going to be taxed in the cases where discount amount is bore by these business entities, which is also known as 'Burn Cost'.

Recommendations

Recently, due to lack of understanding of ecommerce business models, a lot of problems are emerging under indirect tax laws. That is why there is a need of provisions specifically related to ecommerce in the upcoming GST Regime. GST should ensure that taxes are properly and legally levied on the ecommerce transactions. GST is the most crucial step towards the growth of ecommerce sector in India, which should ensure that ecommerce industry would not face the same issues as it is facing in the current tax regime. There are few recommendations:

- A Committee specific to E-commerce should set up, which should have representatives from both government and ecommerce industry side. The committee should understand the various business models present in the market and issues related to ecommerce industry.

- There is no clear definition of ecommerce transactions in current tax regime. Instead of this topics like aggregator or intermediary has been defined and due to the way these topics have been defined there is an ambiguity regarding the taxation of ecommerce transactions. It is highly recommended to define appropriately the ecommerce transactions.
- Under the present taxation framework, ecommerce operators are facing problems from VAT authorities of states as they are asking for VAT from them. This issue has arisen because of lack of understanding about ecommerce business models work. It is recommended to add provisions which should clearly state for which transaction ecommerce operators or suppliers on ecommerce platforms are liable to pay tax. This should be clarified with respect to all basic ecommerce business models existing in cyberspace.
- In case of goods there has been clarification when the selling is inter-state and intra-state, but in case of services there are no such provisions. Because in case of services there can the case where service provider is located in one state and are actually performed in some other state to the person residing in third state. Then which state jurisdiction will prevail? Or whether SGST, CGST or IGST would be applicable in these cases.
- A clear point of taxation should be mentioned, i.e. when taxes has to be discharged for a particular ecommerce transaction. This point of taxation should be mentioned with respect to every stakeholder in a business transaction.

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